No. 80-1203

IN THE

Supreme Court of the United States

October Term, 1980

THE STATE OF NEW JERSEY,

Petitioner

v.

READING COMPANY, et al.,

Respondents

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF FOR READING COMPANY IN OPPOSITION

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QUESTIONS PRESENTED

1. Whether there is any basis for the Court's review of the judgment of the Court of Appeals affirming the District Court's approval of Reading's Plan of Reorganization, which has been successfully consummated under the former Bankruptcy Act.

2. Whether the District Court's approval of Reading's Plan of Reorganization under the former Bankruptcy Act involved an issue under the Tenth Amendment.

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OPINIONS BELOW

The Judgment of the Court of Appeals, affirming the decision and order of the District Court, is found in Petitioner's Appendix at pages 40a-41a. The order of the Court of Appeals, denying New Jersey's petition for rehearing *en banc,* is found in Petitioner's Appendix at pages 42a-43a.

The opinion of the District Court with respect to its approval of the Plan of Reorganization for Reading Company is not yet reported. It is found in Petitioner's Appendix at pages 1a-38a. The order of the District Court, approving the Plan of Reorganization is found in the Appendix at page 39a.

COUNTERSTATEMENT OF THE CASE

Petitioner, State of New Jersey ("New Jersey"), seeks review of the judgment of the United States Court of Appeals for the Third Circuit, which affirmed the opinion and order of the United States District Court for the Eastern District of Pennsylvania ("Reorganization Court") approving the Plan of Reorganization for Reading Company ("Plan") under section 77 of the former Bankruptcy Act, 11 U. S. C. § 205. The Plan was subsequently confirmed by the Reorganization Court and has been successfully consummated and put into effect as of January 1, 1981. Respondent, Reading Company, is the reorganized debtor and successor to the Reading Company Trustees.

New Jersey was the only one of approximately 12,000 creditors and stockholders of Reading to oppose the Plan or seek review of the Reorganization Court's opinion and order approving the Plan. It asserted a claim in the reorganization proceedings below of approximately $250,000 for real estate and corporate franchise taxes, out of a total of over $160,000,000 of claims against the Reading estate.

The Reorganization Court's comprehensive and well-reasoned opinion approving the Plan sets forth the basic structure and terms of the Plan and the context in which it was presented and approved. (A. 1a-9a, 14a-24a) [1] The Plan was patterned after, and addressed many of the same issues as, the earlier plans of reorganization for the Penn Central Transportation Company and the Central Railroad Company of New Jersey which were consummated in 1978 and 1979, respectively. *See In re Penn Central Transportation Company,* 458 F. Supp. 1234

1. References herein to Petitioner's Appendix will be designated as "A. —" and will refer, as above, to its consecutive pagination.

(E. D. Pa. 1978), *aff'd*, 596 F. 2d 1127 (3rd Cir.), *cert. denied*, 444 U. S. 834 (1979); *In re Central R. R. of N. J.*, 473 F. Supp. 225 (D. N. J. 1979). It resolved, through a series of compromises, the complex set of issues and conflicting claims asserted against the Reading estate and was predicated on the belief that such compromises fell comfortably within the range of possible results if all disputed issues were fully litigated. By providing for the issuance of cash and securities to all but current administration claimants, it successfully addressed the uncertainties and delays associated with the recovery of Reading's major asset—the constitutionally-mandated value of its rail properties conveyed to Conrail under the Regional Rail Reorganization Act of 1973, 45 U. S. C. §§ 701-94 (1973) ("Rail Act").[2]

A major compromise of the Plan embraced the claims of state and local taxing authorities. Consistent with settlements reached by the Reading Trustees with other tax claimants beginning in 1978, the Plan provided that real estate tax claims, aggregating both principal and interest, were to be satisfied by the payment of cash in an amount equal to 30% of the claim and the issuance of Series B Administrative Notes in a principal amount equal to 70% of the claim. Corporate tax claims, to the extent allowed by the Reorganization Court, were to be satisfied through the issuance of Series C Administrative Notes. In recognition of the fact that tax claims accrued principally against Reading's rail properties that were conveyed to Conrail, the Series B Administrative Notes are to be paid out of, and are secured by a lien upon, the proceeds of Reading's Valuation Case. The Series C notes will also be secured by a lien upon Valuation Case pro-

2. *See* In the Matter of Valuation Proceedings under §§ 303(c) and 306 of the Regional Reorganization Act of 1973 (Special Court R. R. R. A.), Misc. No. 76-1.

ceeds, but are general obligations of the reorganized company.[3]

In approving the Plan, the Reorganization Court observed that "the competing interests of the contending parties are best served by a consensual plan." (A. 38a) Referring to this Court's decision in *Consolidated Rock Products Co. v. Du Bois,* 312 U. S. 510, 528-30 (1941), the Reorganization Court concluded that the Plan provided appropriate "practical adjustments, rather than a rigid formula." 312 U. S. at 529 (A. 29a-30a). *See also, In re Penn Central Transportation Company,* 596 F. 2d at 1110-11. The court carefully and thoroughly considered New Jersey's objections to the Plan and concluded that "[t]he Plan's treatment of tax claims by payment in cash and securities is a fair and equitable solution" to the difficult and substantial issues involving the validity and priority of tax claims. (A. 27a) It held that deferred taxes properly fell within the meaning of the term "claims" in section 77(b) of the Bankruptcy Act, "the rights of which may be modified by the Plan of Reorganization." (A. 28a)

Following its approval by the Reorganization Court, the Plan was submitted to the vote of, and was overwhelmingly accepted by, Reading's creditors and stockholders pursuant to section 77(e). The Plan was confirmed on September 25, 1980 and on December 23, 1980, the Reorganization Court authorized the Reading Trustees to take the necessary steps to implement the Plan. Distributions of cash and securities of the reorganized company are now being made to its former creditors and stockholders in accordance with the terms of the Plan.

3. Both the Penn Central and CNJ reorganization plans provided for the satisfaction of tax claims through the issuance of cash and notes of the reorganized debtor that were dependent, in part, on the outcome of the valuation proceedings in the Special Court. *See* In re Penn Central Transportation Co., 458 F. Supp. at 1279-80; In re Central R. R. of N. J., 473 F. Supp. at 228-29.

REASONS FOR DENYING THE WRIT

I. The Issues Raised by New Jersey Are Insubstantial and Do Not Require Review by This Court

New Jersey's Petition fails to demonstrate that there are special and important reasons for this Court's review of the orders and judgments below. The Reorganization Court's decision approving the Plan was fully consistent with applicable decisions of this Court and the federal courts of appeals, and did not involve any question of federal law which had not already been settled by this Court. The principles applied by the Reorganization Court and the Court of Appeals were well-established, clear and unambiguous. Moreover, the Plan has now been consummated and the provisions of the former Bankruptcy Act in question have been superseded by the Bankruptcy Code of 1978 11 U. S. C. §§ 101 *et seq.* (1978). New Jersey's Petition for a writ of certiorari should be denied.

New Jersey did not challenge the basic structure of the Plan or oppose the compromise of the claims of others. The compromise of claims in a reorganization, of course, is a long-established practice. As this Court noted in *TMT Trailer Ferry, Inc. v. Anderson,* 390 U. S. 414 (1968), "compromises are 'a normal part of the process of reorganization'." 390 U. S. at 424; *See also, Case v. Los Angeles Lumber Products Co.,* 308 U. S. 106, 130 (1939).

New Jersey has demanded, however, that its own claims be paid entirely in cash. It refers first to the deferral of tax claims during the pendency of the reorganization proceedings below, although it concedes that "the deferral of the current payments of taxes . . . has become the rule in railroad reorganizations." (Brief at 10) *See In re Penn Central Transportation Co.,* 325 F. Supp. 294

(E. D. Pa. 1970) *aff'd*, 452 F. 2d 1107 (3rd Cir. 1971), *cert. denied, New Jersey v. Penn Central Transportation Co.*, 406 U. S. 944 (1972). It then argues that the satisfaction of a portion of its tax claims in high priority securities of the reorganized Reading Company constitutes a further deferral of its tax claims in violation of section 77(e)(3) which, it asserts, required the payment of administration claims in cash.

The Reorganization Court held that administration tax claims could be modified by a plan of reorganization and observed that New Jersey's interpretation of the statute "would allow one 'hold-out' administrative claimant to destroy the carefully interwoven pattern of compromises" upon which the Plan was constructed. (A. 28a) Its holding was consistent with the earlier decision of the Penn Central reorganization court in *In re Penn Central Transportation Co.*, 458 F. Supp. 1234, 1282 (E. D. Pa. 1978), on which it relied throughout its opinion (A. 37a-38a), and with the Court of Appeals' decision affirming the approval of the Penn Central Plan. *In re Penn Central Transportation Co.*, 596 F. 2d 1102 (3d Cir. 1979). No decision of this Court or of another federal court of appeals indicates that the Reorganization Court's decision was incorrect or improper.

New Jersey also argued below that the Plan violated the so-called "absolute priority rule", in so far as it accorded partial cash payments to junior creditors and provided for the satisfaction of a portion of its own tax claims in contingent securities of the reorganized company. The Reorganization Court found, however, that the distribution of cash and securities to tax claimants under the Plan fairly and equitably resolved all questions concerning the validity and priority of tax claims. (A. 26a-27a) With respect to New Jersey's suggestion that the notes of the reorganized company to be distributed to tax claimants

did not represent full payment of its claim because they are payable out of the Valuation Case, the Reorganization Court found that, even with a modest recovery in the Valuation Case, it could reasonably be expected that the notes would be paid in full. (A. 15a) That judgment was fully supported by the record below and was properly endorsed by the Court of Appeals.

The plain intent of section 77, and of the cases which interpreted it, was that in applying the absolute priority rule, reorganization courts would consider the peculiar facts and requirements of each case. *Consolidated Rock Products Co. v. Du Bois,* 312 U. S. 510, 529 (1941) Where, as here, the Reorganization Court made a careful assessment of the extensive record before it and the many factors existing in the reorganization proceedings below, and where its determination that the Plan met all the requirements of the absolute priority rule was affirmed by a court of appeals which is extremely well-versed in cases under section 77, there is simply no need for a re-examination of the issue by this Court.

II. The Reorganization Court's Approval of the Plan Did Not Give Rise to an Issue Under the Tenth Amendment

New Jersey argues that this Court should grant a writ of certiorari to consider its assertion that the Reorganization Court's approval of the Plan violated the Tenth Amendment. The argument is without substance and can be easily dismissed.

The Plan was approved by the Reorganization Court under the federal bankruptcy power which derives from Article I, Section 8 of the Constitution. It has long been established that section 77 was a valid exercise of that power. *Continental Illinois National Bank and Trust Co. v. Chicago R. I. and Pac. Ry.,* 294 U. S. 648, 671 (1935).

The Tenth Amendment does not deprive a federal court of "authority to resort to all means for the exercise of a granted power which are appropriate and plainly adapted to the permitted end." *United States v. Darby*, 312 U. S. 100, 124 (1941). The power of a section 77 court extends to the treatment of tax claims. *Gardner v. New Jersey*, 329 U. S. 565 (1947). In short, the conclusion of the Reorganization Court and the Court of Appeals that the Plan conformed to the requirements of section 77 should put an end to the issue.

Moreover, it is immediately apparent that New Jersey's Tenth Amendment argument utterly fails on the merits. Neither the earlier deferral of its tax claims, nor the manner in which they are being satisfied under the Plan, impairs New Jersey's sovereignty. No action of the Reorganization Court has affected New Jersey's general taxing power or its essential governmental functions. As the Reorganization Court cogently observed below:

> "The deferral of approximately $175,000 of immediate cash payment is hardly disruptive of the day to day functions of an entire state." (A. 32a-33a)

This Court has recognized that even where a limited intrusion upon a state function results from a valid public purpose, such an intrusion does not violate the Tenth Amendment. *National League of Cities v. Usery*, 426 U. S. 833, 852-53 (1976); *Fry v. United States*, 421 U. S. 542, 547-48 (1975). The Reorganization Court clearly had the power to authorize the deferral of New Jersey's tax claims to permit continued rail operations by Reading in the public interest. *In re Penn Central Transportation Co.*, 452 F. 2d 1107 (3d Cir. 1971), *cert. denied*, 406 U. S. 944 (1972). If New Jersey must now accept a form of compensation other than cash for the remaining balance of its claim, it is only to effectuate the valid purposes of the statute under which the Plan was approved.

CONCLUSION

For all of the reasons stated above, New Jersey's Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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February 18, 1981